# International Updates

## Six Countries Meet

Each year, senior officials from six English-speaking countries-Australia, Canada, Ireland, New Zealand, the United Kingdom (U.K.), and the United States-who are responsible for their countries' social security system meet to discuss topics of common interest within the programs. This year's meeting took place September 2 l-26, 1997, in Dublin, Ireland.

While specific concerns differ from country to country, all of them must deal with the growing problem of meeting the needs of an aging society in an environment of financial constraints. Interestingly, while the five countries under review have held national elections recently, and all except Canada's election resulted in a turnover of power to the former opposition, the adjustments being made to prepare social security programs for the future generally display a strong degree of continuity (see chart I).

The following sections provide an overview of each country's social security system, with an emphasis on retirement benefits, and include a summary of recent program developments.

## Australia

The Australian retirement system is essentially supported by two independent pillars. The first pillar is a *means-tested public pension* entirely financed from general revenues. This program also partially subsidizes pharmaceutical expenses, medical (including hospital and nursing home) costs, and grants that defray public hospital operating expenses for each of Australia's six states and two territories. However, insured persons pay part of the cost of medical benefits if taxable income exceeds A$2 1,366 (plus A$2,100 per child) a year for couples and single parents, or A$12,688 if single without dependents (US$1 .OO = A$1.35) and employers pay the whole cost of work injury benefits.

The second pillar, established in 1991, might be considered a form of privatized social security. Although this program is Government mandated, it consists of a *privately managed employer-funded retirement scheme.* Employers are free to choose which fund to invest in. Under this second-pillar scheme, private sector coverage of Australian employees has risen from 30 percent to 90 percent.

The present retirement system has its origins in a political agreement reached by Australia's labor unions with its then Labour government in 1986 to increase overall compensation at the rate of inflation, with half to be paid in the form of a retirement fund contribution. This arrangement addressed several important problems simultaneously.

- It enabled unions to gain a large compensation increase without creating new inflationary pressure.
- It addressed the retirement concerns of Australia's aging population without adding to the Government's fiscal burden.
- It was viewed as a way to increase national saving and growth.

The retirement pension (superannuation) scheme is being phased in over 10 years. Starting with the 3-percent requirement imposed in 1992, the employer contribution will rise to 9 percent by 2002. Toward the end of the period, a 3-percent employee contribution will be added, bringing the total rate to 12 percent. This is expected to be financed through the politically difficult task of holding the line on wage hikes as productivity grows. For example, a 1 -percent annual increase in productivity would cover superannuation costs while keeping real take-home pay roughly constant.

The objective is to entirely or substantially replace Government old-age pensions. However, since accumulated contributions can be accessed at age 55—as either a lump sum or annuity-there is a strong incentive for low- and middle-income earners who cannot expect to accumulate superannuation much above their guaranteed Government pensions, to retire early and withdraw their savings as lump sums. Consequently, about 70 percent of the retirement-age population still receive old-age benefits.

Moreover, because all workers in a firm must be in the same fund with a single investment strategy, there is the potential for conflict between young and old workers with different financial time horizons and/or between individual workers who have different proclivities (some are more risk-averse than others).

### Legislation

The Liberal-National Government that was elected in 1996 after a 14-year absence from power, has redirected these policies somewhat towards a greater emphasis on tax rebates,

Chart 1 .-Comparison of social security programs amongst six English-speaking countries, by demographic characteristics, 1997

| Demographic characteristics | Australia | Canada | Ireland | New Zealand | United Kingdom | United States |
|---|---|---|---|---|---|---|
| Mid-1997 population (in millions) | 18.5 | 30.1 | 3.6 | 3.6 | 59.0 | 267.7 |
| Annual population increase (in percents) | .7 | .5 | .5 | .8 | .2 | .6 |
| Population doubling time at current rate (in years) | 100.0 | 127.0 | 147.0 | 86.0 | 433.0 | 116.0 |
| Projected 2010 population (in millions) | 20.8 | 33.6 | 3.7 | 4.0 | S8.6 | 297.7 |
| Percent of urban population | 85.0 | 77.0 | 57.0 | 85.0 | 90.0 | 75.0 |
| Life expectancy at birth | | | | | | |
| Male | 75.0 | 75.0 | 73.0 | 73.0 | 74.0 | 73.0 |
| Female | 81.0 | 81.0 | 79.0 | 79.0 | 79.0 | 79.0 |
| Total fertility rate | 1.8 | 1.6 | 1.9 | 2.0 | I.7 | 2.0 |
| 1995 per capita gross national product in US dollars | $18.720 | $19.380 | $14,710 | $14,340 | $18,700 | $26.980 |
| Average annual (I 985-95) real growth rate of per capita gross national product (in percents) | 1.4 | .4 | 5.2 | .6 | 1.4 | 1.4 |
| Average annual inflation rate. 1985-95 | 3.7 | 2.9 | 2.5 | 3.9 | 5.1 | 3.2 |
| Percent of population under age I5 | 21.0 | 20.0 | 25.0 | 23.0 | 19.0 | 22.0 |
| Percent of population aged 65 or older | 12.0 | 13.0 | 11.0 | 12.0 | 16.0 | 13.0 |
| Dependency ratio (in percents) [1] | 51.0 | 49.0 | 51.0 | 53.0 | 55.0 | 53.0 |
| Activity rate 1995 (in percents) [2] | 64.0 | 65.0 | 53.0 | 65.0 | 44.0 | 67.0 |
| Percent of women in the labor force (1995) | 43.0 | 45.0 | 33.0 | 44.0 | 43.0 | 46.0 |
| Statutory pensionable age | | | | | | |
| Male | 65.0 | 65.0 | 66.0 | 63.0 | 65.0 | 65.0 |
| Female | 61.0 | 65.0 | 66.0 | 63.0 | 60.0 | 65.0 |
| Types of OASDI programs | | | | | | |
| Contributory flat rate | | | X | | X | |
| Contributory earnings related | | X | | | [3] X | X |
| Noncontributory means-tested | X | X | X | X | X | X |
| Noncontributory flat-rate universal | | X | | | | |
| Mandated private pension | X | | | | | |

[1] Population aged 0-14 plus population aged 65 or older, divided by population aged 15-64.

[2] Total population aged 15 or older who are economically active.

[3] With contracting-out options.

support for home carers, and incentives to encourage work beyond the current retirement age of 55. The Government recommended in its 1997-98 budget, a tax rebate of 7.5 percent from July I, 1998, on the first A$3,000 earned from any form of savings, investments, or superannuation contributions made by employees or the self-employed, rising to 15 percent from July 1, 1999. This replaces a 3-percent Government co-contribution to superannuation payments by low- and mid-income earners that had been promised by the previous Labour Government.

*Superannuation contributions and termination payments surcharges.-In* April of this year, five bills were introduced to reduce the trend toward early withdrawal by imposing a superannuation contributions surcharge and a termination payments surcharge for high-income earners. These surcharges follow on provisions in the 1996 budget allowing low-income earners not to contribute to their employer designated pension funds, and imposing a 15-percent levy on the rich (defined as persons with incomes over A$85,000).

*Weekly benefits* increase.-Effective March 1997, the weekly rate for old-age pensions has been increased slightly. Pension payments must now be no less than 25 percent of the average weekly earnings for males.

Exemptions.-Exemptions to apply when means testing social security recipients aged 55 or older were announced on July 15, 1997. These will apply when the asset is inaccessible because of a contract entered into before the 1996 budget announcement, or because of the rules of the superannuation fund-for example, cases where the customer purchased a traditional *endowment* or *life* contract or a fixed *term rollover* that is inaccessible until the end of the contract period before the budget announcement, or access to the asset is legislatively barred. Unemployed persons who are not yet retired will be able to access their superannuation on grounds of financial hardship (subject to the rules of fund).

*Deferred pension bonus* plan.-Persons who delay retirement will receive a tax-free bonus payment amounting to 9.4 percent of pension entitlement for each full year of work (up to 5) beyond the age pension qualifying age. The maximum bonus will be A$2 1,250 for a single person and A$35,450 for a couple.

*National carer action* plan.-Effective July 1, 1997, the Government relaxed the rules for receiving carer payment (previously known as carer pension). This is payable to a person providing constant care on a long-term basis to a social security pensioner who has a severe disability or who is frail and aged; the carer must live in, or adjacent to, the recipient's home. Carers can now take part in 20 hours of training or voluntary work each week and the number of days of break from caring (respite days) has increased from 42 to 52. Effective July 1998, respite days will rise further to 63, and carer payment eligibility will extend to persons caring for a child under age 16 with a profound disability, or who are required to care for an adult as well as that adult's dependent child.

## Canada

Uniquely among the five countries under discussion, Canada's Federal general election in June did not result in a change of Government. Early in 1994, a newly created Standing Committee on Human Resources Development had been charged to define issues, concerns, and priorities and to develop an action plan for a general reform affecting all aspects of social welfare (including taxes) and laws relating to education, labor, and private pensions. All forms of social assistance and income security programs were to be considered. The re-elected Liberal Government is continuing this process.

Canada's social security system has six components divided between federally and provincially administered programs:

1) The *Canada Pension Plan* (CPP).-A Federal, contributory, earnings-related insurance program providing old- age, survivor, and disability benefits ` (Quebec has its own separately administered, parallel *Québec Pension Plan* (QPP));

(2) *Old-Age Security* (OAS).—A Federal, noncontributory, universal program linked to two means-tested programs to provide old-age and widow or widower allowances;

(3) *Employment Insurance* (EI).-A Federal, contributory, earnings-related insurance program providing cash benefits for sickness, maternity, and unemployment;

(4) *Child Tax Benefit* (CTB).-This benefit is related to the Federal income tax providing assistance for families with children;

(5) *National Health Cure.-A* universal, federally mandated, provincially administered program; and

(6) *Workers' Compensation.-A* set of province-level programs.

General revenues finance the whole cost of noncontributory programs (means-tested or not). Employers and employees finance the contributory social insurance programs, including CPP/QPP and employment-related insurance for sickness, maternity, and unemployment. The national health service is financed by the provincial governments and by block grants from the National Government. In addition, employer and employee contributions are required in some Provinces, and are optional in others, where union contracts determine premium amounts. Employers pay for the whole cost of Provincially mandated compensation for worker injuries.

The CPP was first introduced in 1965 to provide earnings-related old-age, disability, and survivors benefits. Benefits were first paid in the late 1970s. The normal retirement age is 65, when benefits are payable at 25 percent of average covered earnings. A maximum of 15 percent of low-income years may be disregarded, plus years spent caring for a child under age 7. The old-age pension may be taken at age 60, with benefits reduced by one-half percent for each month the recipient is underage 65; an increment of one-half percent for each month of deferral is payable until age 70.

The disability benefit under the CPP consists of a flat amount plus 75 percent of what the retirement pension would have been (up to a maximum). The survivor benefit amounts to 60 percent of the retirement pension of the deceased, payable to the widow or widower at age 65 or older; the benefit is reduced if the widowed spouse is under age 65. Orphan's benefits are paid in flat amounts.

OAS is a universal, noncontributory old-age benefit that provides basic, first-tier income to all Canadians aged 65 or older, whether retired or not. The major requirements are age and at least IO years of residence in Canada after age 18. Benefit amounts are adjusted quarterly for price increases. The maximum monthly benefit for July through September 1997 is C$405.12, (about US$302) payable to residents of 40 years or more.

OAS is not means tested. However, since 1990 pensioners with a net income from all sources in excess of a certain amount (C$53,2 15 in 1997) are subject to *cluwback-they* must repay all or part of their basic OAS benefit through personal income tax. Repayment is 15 percent of such excess income, resulting in full recovery of single recipients' benefits at an income of around C$85,000. Couples with incomes of up to C$170,000 or more may continue to be paid benefits.

In addition, means-tested supplements are available for OAS pensioners who live in Canada and have little or no other income. The Guaranteed Income Supplement (GIS) program provides for extra payments to all OAS recipients whose incomes are below certain limits. The amount of GIS is a function of personal income and marital status. In 1997, maximum annual payments for OAS and GIS combined provide around C$10,600 for single recipients and C$17,200 for a couple. Spouses and widow(er)s of OAS pensioners, aged 60-64 with little or no income are eligible for a spouse's allowance (SPA) that is equivalent to an OAS and GIS payment combined. Several provinces and territories supplement GIS and SPA benefits.

EI provides cash benefits for sickness, maternity, and unemployment. The current law, enacted in 1996 after 2 years of consultations, resulted in major changes to the previous law. At present, benefits are payable up to 15 weeks for sickness and maternity, or up to 45 weeks for unemployment (depending on unemployment rate in the region and the individual's employment history) at a base rate of 55 percent of average insured earnings adjusted by the local unemployment rate and subject to a flat-rate maximum. Beneficiaries with a net taxable income greater than C$48,750 who have received less than 21 weeks of benefits in the last 5 years are generally required to pay back up to 30 percent of their benefits. Those who have received 21 or more weeks of benefits over the period are subject to clawback when net taxable income for the following year exceeds C$39,000. The repayment depends on how many weeks benefits were paid in the past 5 years, and can equal up to 50-l 00 percent of benefits received in a given year.

The CTB provides income-tested monthly tax-free payments to families with children. Benefits decrease as net family income increase and reach zero, at an annual net income of about C$66,700 for one- and two-child families. At present, some payment is made to 85 percent of all Canadian families with children.

The national system of health care is characterized by full portability, accessibility, and universality. The Federal government sets minimum standards for levels of health care, but the programs (known to Canadians as *Medicare)* are operated independently by the provinces and territories. The system provides comprehensive health care to the population. In some provinces, this includes the provision of such additional benefits as nursing home care, dental care, and drugs.

Work injury programs vary widely by province or territory, but all are employer financed and pay temporary as well as permanent benefits, with no minimum period of coverage, and provide medical and rehabilitation care as well as funeral grants.

With an aging population, increasing medical costs, and other social and economic challenges, Canadians have been reassessing these programs.

- The CPP has been revamped and the revised program is on the verge of implementation. Proposed legislation represents agreement reached by the Federal and Provincial governments after a year-long process of consultations with the Canadian public. Among the principal features are a considerably accelerated increase in the joint worker/employer contribution rate, freezing a year's basic exemption at the 1998 level, and diversi fying the CPP investment portfolio. Changes will not apply to current CPP pensioners or anyone born before 1933.

- EI has replaced the former Unemployment Insurance. A major liberalization involves counting hours worked instead of requiring a weekly minimum income. This allows more part-time employees to earn insured status. There are also provisions to allow low-income earners receiving a child tax benefit to receive a higher EI benefit. The new laws, however, generally reduce benefits. A lower benefit percentage and a payback increase for higher income earners apply. There is also a provision lowering the income replacement rate for persons with repeat claims. The second part of the new law targets job creation and support for reemployment programs.

- On the horizon is a Seniors' Benefit, which would replace the current OAS and GIS benefits. The Federal Government's proposal calls for implementation in 2001. Under the new program, recipients would be means tested but their benefits would be tax free, eliminating the present clawback provisions.

## *Ireland*

The public social security system in Ireland consists of four components:

(1) *Contributory social* insurance.-Provides old-age, survivors, and disability pensions; plus cash benefits for sickness, maternity, unemployment, and work injury;

*(2) Noncontributory social insurance.*- Provides universal child benefits and allowances for specified conditions provided after a means test;

(3) *A special pension system for public employees;* and

*(4) Free comprehensive hospital and medical care.*— Available to low-income residents and limited services to remaining residents.

Private pensions provide the only earnings-related retirement income.

Social insurance is funded by a single payroll tax from employers and employees, with employers contributing at a higher rate. Funding is on a pay-as-you-go basis; general revenue subsidies cover any operating deficit (less than 2 percent in 1995). Noncontributory benefits are paid out of general revenues. Contributory benefits account for almost 40 percent of total social welfare expenditures, excluding those for civil servants, with means-tested benefits accounting for over 40 percent and nonmeans-tested benefits accounting for more than 10 percent in 1995.

Participation is compulsory for all employed persons aged 16-65 earning I£30 (US$50) or more per week. The self-employed are covered only for the Old Age (Contributory) Pension and Widow's and Orphan's (Contributory) Pensions. Public employees, domestic workers, and some part-time workers are excluded.

A person may receive either of two different kinds of flat-rate weekly benefits (with identical amounts) because of old age: a *retirement pension* payable at age 65 if no longer in full-time employment; or an *old-age contributory pension* payable at age 66 without a retirement test. To receive the maximum, a pensioner must have at least 156 weeks of payroll contributions, a yearly average of at least 48 weeks of paid or credited contributions, and have started working before attaining age 55 for a retirement pension, or age 56 or 57 for an old age contributory pension. Those averaging between 48 and 24 weeks of contributions annually receive a proportionately reduced benefit. Weekly supplements are payable for an adult dependent or dependent children. Additional benefits are also paid to pensioners living alone or aged 80 or older.

A flat-rate permanent disability pension is payable if the pensioner has 260 weeks of paid contribution and 48 weeks of paid or credited contributions in the last complete income tax year.

Noncontributory allowances available to low-income residents under specified conditions include pensions for old-age, widows, and orphans; allowances for the unemployed and for long-term (15 or more months) unemployed older (55-64) workers; and benefits for single parents, care givers, blind persons, and other disadvantaged groups with limited assets. Child benefits are the only noncontributory benefit not subject to an income or means test. They are granted to children under age 16 ( 17 if student or disabled). In some cases there are offsets, depending on program regulations. All noncontributory benefits are flat-rate, paid weekly, and financed from general revenues.

*Voluntary private pensions* provide the only earnings-related income for retirees. Pension coverage in the private sector grew from 27 percent of employees in the mid- 1970s to almost 40 percent by 1985. The trend, however, has turned into a modest decline in the last decade, according to a 1995 survey. While Irish pension fund assets have increased from about 17 percent of the gross national product in 1985, to an impressive 45 percent in 1995, only 38 percent of employees in the private sector were covered. Coverage was concentrated in better paid and more secure employment, such as industrial and large service firms and building and construction, as well as the public sector with its own program. Only 27 percent of the self-employed are covered, 16 percent of those who work for small businesses, and 10 percent of part-time or temporary staff. Moreover, women are significantly less likely to be covered than men.

The basic framework of Ireland's social security system has remained largely unchanged for over two decades. However, following the pension coverage survey in 1995, the Government launched a National Pensions Policy Initiative to find the most appropriate methods of ensuring that workers are adequately protected in their retirement. The National Pensions Board is preparing recommendations by the end of this year for long-range changes in the private and public pension systems, with the objective of covering more of the working population.

Recent Government policies aim to balance the need to ensure an adequate income for all against the equally important objective of providing strong and clear incentives to work. Since taking office in June 1997, the new coalition Government (comprising the Fianna Fail and Progressive Democrats, with support from several independent members) has not suggested any change in the social policy initiatives laid down by its Fine Gael-Labour-Workers' Party predecessor. Taking advantage of several years of continuing economic growth, the 1997 budget and a subsequent social welfare bill announced comprehensive benefit improvements for pensioners, families, children, and carers of children or the disabled, plus measures designed to encourage welfare recipients to return to work. For example, there is an additional 50 percent payment to those providing care to more than one person; and the means-test threshold is also to be relaxed. The estimated annual cost of these improvements will be I&215 million (US$358 million).

## *New Zealand*

All residents in New Zealand have coverage under five branches of social security:

(1) an old-age survivors and disability program;
(2) cash sickness benefits and medical care;
(3) accident compensation for both work and nonwork related injuries;
(4) unemployment benefits; and
(5) family allowances.

General revenues fund medical care and (unlike most countries) all cash benefit programs except accident compensation.

All benefits (except cash benefits for work injury) are paid in flat-rate amounts, and most are adjusted once a year according to the lesser of increases in prices or average wages. The old-age benefit now payable to residents at age 62.9—the pensionable age is rising gradually to 65 by the year 200 l-is NZ$249.50 a week for a single person living alone, and NZ$368.66 for an aged couple; after taxes, NZ$203.53 and NZ$3 13.12, respectively. (NZ$1 .OO = approximately US$1.40). The single rate equals about 55 percent of the national average wage. There is a special income tax surcharge of 25 percent for beneficiaries whose nonbeneft taxable income exceeds certain limits.

Eligibility for most social security benefits is based on age and residency and not related to employment or contingent on contributions. An additional direct income test applies for disability and survivor benefits, cash benefits for sickness and maternity, and unemployment benefits.

Disability benefits are payable at rates somewhat lower than old-age pension levels to residents who have permanent or severe incapacity or are totally blind. Accident insurance provides up to 80 percent of earnings according to degree of incapacity, regardless of whether the injury is work related. Cash benefits for sickness and maternity are payable to gainfully employed persons with only limited incomes.

Supplementary flat-rate benefits, some needs-tested, are payable for housing, for home maintenance and repairs, and as special needs grants to old-age, disability, and survivor pensioners.

Unemployment benefits, income-tested and financed by general revenue, are payable to residents after a waiting period of 2 to 10 weeks.

A national health care program provides residents free care in public hospitals. Most other medical services involve modest cost sharing. Only minimal fees are required of the poor or chronically ill.

### *Proposed Compulsory Saving Scheme*

At the initiative of the National-New Zealand First coalition that took office last October, a retirement savings scheme (RSS) was being voted on by the citizens of New Zealand (through the mail) during the month of September. This was designed to move the New Zealand system substantially in the direction of privatizing its social security system. If approved, RSS would be implemented in 1998 for individuals with annual earnings above NZ$5,000. Each person would choose a private sector fund which will invest contributions. The contribution rate would begin at 3 percent of earnings and will gradually increase to 8 percent within 5 years, provided that the government institutes tax cuts offsetting the increased cost of RSS to the individual.

At age 65 a person would purchase a tax-free annuity which would start paying 33 percent of average net wages for a single person and 66 percent for a married couple, adjusted annually according to changes in the consumer price index. When savings are not sufficient to purchase such an annuity at age 65—because of family commitments or low income-the Government would make up the difference between actual savings and the purchase amount. In addition, since women live longer than men on average, the market now charges women a higher price for a lifetime annuity. The Government would give all women, regardless of the amounts they have saved, any additional amounts needed to buy annuities equivalent to those of men.

Persons born before April 1, 1938. would not join RSS and instead continue to receive full benefits under the current scheme, New Zealand Superannuation (NZS). Since NZS would be phased out between 2003 and 2038, those born after April 1, 1973, would receive all their retirement income from annuities; everyone born between the cutoff dates would receive retirement income from both sources, with older workers receiving a higher proportion of their retirement benefits from NZS.

(Although praised by financial experts, the proposal was received skeptically by the general public. As this note went to press, it was announced that the proposal had been rejected by an unexpectedly large margin. Some 92.4 percent of those voting were opposed.)

## *The United Kingdom*

The British social security system consists of three components:

(1) *Contributory social insurance* (National Insurance, or NI).-A two-tier program providing old-age and survivors pensions, and cash benefits for disability, maternity, unemployment, and work injury;

*(2)* Two types of *noncontributory programs.-One* program is means-tested and the other is non-means-tested. Both serve as a basic safety net; and

*(3) A health care* service.-This service furnishes comprehensive hospital and medical care, as well as the reimbursement of many medical expenses.

Social insurance is financed on a pay-as-you-go basis by a single payroll tax from employers and employees, with employers contributing at a higher rate. The Treasury may cover shortfalls with grants up to 17 percent of total benefit costs, Expenditures for contributory programs account for about half of total social welfare costs.

Participation in the first *contributory* tier is compulsory for all persons above the *lower earnings level* (about 15 percent of gross male average earnings per week as of April 1995). About 12 percent of employees are excluded on account of low earnings. Benefits are flat-rate weekly amounts for both long-term (old-age and permanent disability) and short-term (temporary disability, maternity, unemployment, and work injury) contingencies, based on years of contribution independent of earnings. The second, *earnings-related tier* (the *State Earnings-Related Pension Scheme*, or SERPS) covers only employees who choose not to contract out to occupational or personal pensions. The self-employed are excluded, but may establish personal pension plans on their own.

### Contributory Social Insurance

The Old-Age and Survivors Insurance pension is part of the contributory program. It consists of a flat-rate weekly basic benefit and an earnings-related amount under SERPS. (The contributory disability pension provides flat-rate basic benefit only.) Two-tier old-age benefits are payable at age 65 for men and 60 (to be raised to age 65 between 2010 and 2020) for women.

To receive the maximum *first-tier* benefit (about 15 percent of the gross male average wage), the pensioner must have contributions in 9/10ths of the years of *working life (49* years for men, 44 years for women, with provisions for nonworking years due to unemployment, disability, or caring for children or the disabled). The amount is reduced proportionately for shorter coverage; no pension is payable if the proportion is less than 25 percent. An additional 7.5 percent (10.4 percent starting in 2010) of the basic benefit is paid for each year of deferred claim up to age 70, but this age limit will be dropped starting in 20 10. There is no option for receiving a reduced pension before the pensionable age. Survivor benefits with supplements for dependent children are provided; benefit amounts vary according to the ages of the survivor and dependents.

The maximum *second-tier* SERPS earnings-related pension is set at 25 percent of covered earnings in the best 20 years. Those reaching pensionable age after April 6, 1999, will be subject to a phased-in reduction until the maximum falls to 20 percent of *working life* earnings by April 2009. Survivor benefits are payable based on the deceased spouse's earnings. Both flat-rate and earnings-related benefits are subject to income tax, and there are no earnings or income tests for either of the benefits. A special *old-person's pension* guarantees a specified weekly amount to those aged 80 or older who would otherwise receive less or no pension.

### Noncontributory Social Insurance

Noncontributory benefits are paid out of general revenues, with *means-tested* benefits about a third, and other noncontributory benefits about a sixth of total social welfare expenditures. All benefits are flat-rate and paid weekly. Means-tested benefits are available to low-income residents for general living expenses (income support, family credit, and disability working allowance); housing subsidies (housing benefit and council tax benefit); and specific expenses (free school meals, National Health Service Low Income Scheme, and Social Fund).

*Nonmeans-tested* benefits are payable on the basis of special circumstances, regardless of other income (for example, war pensions, allowances for the disabled, and universal child benefits).

Virtually all the IO million individuals of pensionable age receive a basic NI pension from the state. Of these, some 4 million persons also receive SERPS, and about 6 million receive an occupational pension. Three million persons also receive means-tested benefits and allowances. It is estimated that a considerable number of eligible pensioners have not applied for means-tested assistance. Personal pensions will not have much effect until the first cohort who took them out in large numbers begin to retire, starting around 2026.

### Contracting-Out of the State Earnings-Related Pensions

Provisions for employers to *contract out* of the public pension with occupational plans were made when the U.K. introduced its first earning-related pension scheme-the *graduated pension-in* 196 1. When a subsequent social security law replaced it with SERPS in 1978, the new law encouraged contracting-out by requiring that alternative pension plans must provide a *guaranteed minimum pension* (GMP) at least equal to those under SERPS, with any added costs for keeping the GMP in line with prices to be borne by the NI fund instead of the private pension plans. It also provided rebates for contributions to occupational plans.

Reforms in the 1986 Social Security Act dramatically changed the way public and private pensions supplement the basic flat-rate state pension. Beginning in 1988, all members of the contracted-out occupational schemes, which are mostly defined benefit plans, and those covered by SERPS have been free to opt out either wholly or in part by starting a personal defined-contribution pension plan. The role of private pensions has since increased rapidly, and the number of SERPS members has fallen. As of 1991, about 5 l percent of all covered employees had contracted out through membership in occupational pension schemes; and an additional 28 percent on the basis of personal pensions. Only 14 percent (about 2.5 million employees) had SERPS as their sole supplementary pension, and 6 percent had both SERPS and additional occupational pension coverage.

Recent social security policies have aimed to cut Government spending by reducing its role in old-age pensions, encouraging contracting-out of the SERPS, tightening qualifying conditions for disability pensions, and subjecting the unemployed to more stringent tests. On the whole, Government policies focus on directing resources toward means-tested benefits to help those without other income. These policies are, in general, continuing under the incoming Labour government elected in May.

### *Incapacity Benefit (IB)*

As of April 1995, the IB replaced State cash benefits for sick leave and the disability pension by introducing a more stringent work test that may remove 1/6th of disability beneficiaries from the rolls. New claimants who would previously have been paid on the grounds that they are unable to do their *former* jobs will now be disallowed unless they cannot do any *reasonable* job. Ability to do so is now assessed by specially trained doctors using a functionally based methodology in place of relying on reports from the applicants' own General Practitioners. For new beneficiaries, the IB will be taxable after the 28th week. In addition, flat-rate disability allowances have been reduced, and earnings-related SERPS disability benefits have been eliminated.

### *Unemployment Benefit (Job Seeker's Allowance)*

Effective April 1996, a new *Job Seeker's Allowance* replaced the contributory NI unemployment benefit and means-tested cash benefits for the low-income unemployed. The flat-rate unemployment benefit is payable for 6 months rather than 1 year, and the dependent supplement for a nonworking adult is abolished.

### *Contracted-Out Supplementary Pensions*

The 1995 Pension Act (effective April 1997): (1) eliminated the requirement for defined-benefit plans to provide at least the *guaranteed minimum pension,* relieving the NI of the obligation to keep GMP payments in line with price increases; (2) introduced *age-related rebates* to employees participating in defined-contribution plans, ranging up to 9 percent for older participants, as an incentive to remain in contracted-out plans; and (3) established *safeguards for funding and fund operations* to provide compensation for misuse and mismanagement of pension funds.

### *Prospects for Public and Private Pensions*

The cumulative impact of the 1986 and 1995 pension laws will render both flat-rate and earnings-related public pensions insignificant within four decades, according to some analysts. They point to three developments: (1) a dwindling in the basic flat-rate state pension relative to earnings (as a result of price indexing since November 1980); (2) a phased-in cut (beginning 1999) of the maximum SERPS pension from 25 percent of covered earnings in the highest-earning 20 years, to 20 percent of covered *working life* earnings; and (3) a technical revision (enacted by the 1995 law) in how past earnings are computed when SERPS benefits are calculated, resulting in somewhat lower benefits beginning in 2000 and substantial savings to the system by 2050.

The defined-contribution pension plans have become more popular than before among employers offering contracted-out occupational pensions. Personal pensions are increasingly substituting for SERPS and, to a certain extent, occupational plans. The Government's recent revocation of tax credits on dividend income starting July 1997 may be a disincentive for employers to offer defined-benefit plans, or to provide any pension plans at all.

The incoming Government has launched a review of pensions policy, promising a proposal on the subject in early 1998. It plans to keep the basic (flat-rate) state retirement benefit intact, while considering new *stakeholder pensions* with low administrative costs as an alternative to SERPs or personal pensions for those who have low and modest incomes or sporadic work histories and are thus excluded from occupational pensions. SERPS would be kept for those who wish to remain within it. Also under consideration is a new *citizenship pension* for about 7 million persons who are not in paid work (mostly caring for children or disabled), perhaps with the Government paying their NI contributions.

There is a growing Government concern that workers earning below-average wages may suffer losses in retirement income by opting out of SERPS for personal pensions due to the latter's relatively high administrative costs. To counter criticisms of misleading tactics used by independent financial advisers as well as major insurance firms to sell personal pensions since 1988, of a lack of safeguards for unsuspecting investors, and of ineffective mechanisms for redress, the Government has implemented new regulations to certify personal pension policies, and announced plans to review the current self-regulatory structure, scheduled for completion by the end of 1998. Under consideration is the establishment of a *super regulatory agency,* as a new and fully statutory system to replace the existing mechanism.

-Martynas Ycas